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In the Supreme Court of the United States

OCTOBER TERM, 1951

No. 221

C. E. KING AND JUANITA M. KING, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Court of Appeals (R. 97-100) is reported at 189 F. 2d 122. The findings of fact and opinion of the Tax Court (R. 29-35) are unreported.

JURISDICTION

The judgment of the Court of Appeals (R. 100) was entered on May 22, 1951. A petition for rehearing (R. 101-112) was filed on June 7, 1951, and

was denied on June 29, 1951 (R. 114). The petition for a writ of certiorari was filed on August 2, 1951. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254.

QUESTION PRESENTED

Whether the Tax Court erred in holding that certain houses were held in 1946 by the taxpayer primarily for sale to customers in the ordinary course of trade or business within the meaning of Section 117(a)(1) and (j)(1) of the Internal Revenue Code, and that the gain thereon should therefore be treated as ordinary income rather than as capital gain.

STATUTE INVOLVED

Internal Revenue Code:

> SEC. 117. CAPITAL GAINS AND LOSSES.
>
> (a) [as amended by Section 115(b) of the Revenue Act of 1941, c. 412, 55 Stat. 687, and Section 151(a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Definitions.*—As used in this chapter—
>
> (1) *Capital Assets.*—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to cus-

tomers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23(l), or an obligation of the United States or any of its possessions, or of a State or Territory, or any political subdivision thereof, or of the District of Columbia, issued on or after March 1, 1941, on a discount basis and payable without interest at a fixed maturity date not exceeding one year from the date of issue, or real property used in the trade or business of the taxpayer;

* * * * *

(j) [as added by Section 151(b) of the Revenue Act of 1942 and amended by Section 127(b) of the Revenue Act of 1943, c. 63, 58 Stat. 21]. *Gains and Losses from Involuntary Conversion and from the Sale or Exchange of Certain Property Used in the Trade or Business.*—

(1) *Definition of Property Used in the Trade or Business.*—For the purposes of this subsection, the term "property used in the trade or business" means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23 (l), held for more than 6 months, and real property used in the trade or business, held for more than 6 months, which is not (A) property of a kind which would properly be includible in the inventory of the taxpayer if on hand at the

close of the taxable year, or (B) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business. Such term also includes timber with respect to which subsection (k) (1) or (2) is applicable.

* * * * *

(26 U.S.C. 1946 ed., Sec. 117.)

STATEMENT

The facts as found by the Tax Court (R. 30-34) are as follows:

J. L. Martin Investment Company was a Texas corporation formed in 1942, 50 per cent of whose stock had been acquired by the taxpayer, C. E. King, in that year.[1] Later, in July, 1945, the taxpayer acquired the remaining 50 per cent, so that at that time he owned all of the stock of the corporation. (R. 30.)

In 1942 and 1943, the corporation built 320 houses in Texas City, Texas, under an F.H.A. approved housing plan, on two lots. Fifty of these houses were built in one project and 270 in another several blocks away. The houses were constructed for rental purposes, and all of them were rented. (R. 31.)

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[1] Throughout this brief, reference will be made only to the taxpayer, C. E. King, whose activities are alone here in question. The taxpayer, Juanita M. King, was C. E. King's wife and returned one half of his earnings as her share of the community earnings.

Certain of the houses so built were rented with an option to purchase. After the taxpayer became the president of the corporation on January 1, 1943, a letter, dated June 21, 1942, was addressed by the corporation to the occupants thereof stating that it was the corporation's desire to sell the property and that it would be glad to have the occupant exercise such option. A follow-up letter was addressed to each occupant in which it was stated that the corporation preferred to sell rather than rent, and that it would hold the option open for another five days. (R. 32.)

During 1944, six houses were sold by the corporation (R. 32).

The houses were of poor construction, substitute materials and untreated lumber being used; there was no steel mesh in the concrete slabs; galvanized wire instead of copper was used; plastic was used for trim and fixtures, and paint which was applied with spray guns peeled off in a few months, especially on the windward side. (R. 32.)

The corporation had always shown an operating loss (R. 32); and when, in July 1945, the taxpayer bought the remaining 50 per cent of its stock, so that he then owned all of it, the company was liquidated. All of its assets, including 291 of the houses then owned by the corporation, were transferred to the taxpayer, the balance of 29 houses having theretofore been sold by the corporation. (R. 31.)

The taxpayer owned minority stock interests in two or three corporations engaged in subdividing

and selling property, and his business had at all times been real estate and the handling of rental property, but he had never had a broker's license (R. 32).

At the time the taxpayer acquired the corporation's properties in 1945, he had the thought in mind of selling them and reinvesting the proceeds in other property. He consequently made an unsuccessful effort to sell them on a wholesale basis (R. 34).

In 1945, F.H.A. was urging that the houses be sold and, on these instructions, extensive and strenuous efforts were made by the taxpayer to sell them. His local manager was offered a bonus on sales that he might make; the houses were advertised for sale, and all kinds of inducements were made to get buyers. (R. 33.)

On July 2, 1945, letters were addressed to all tenants urging them to buy the houses and offering to give them the five per cent commission ordinarily paid to salesmen. These letters were followed up by letters of July 29, 1945, again urging the tenants to buy the houses. All of the tenants were approached either by personal letters or interviews. A strenuous house-to-house sales effort was made in August, 1945. (R. 33.)

In 1945, the taxpayer sold two houses (R. 33) and in 1946, that is, in the taxable year here in question, after the home purchasing program for veterans went into effect, the taxpayer sold 49 of them

(R. 31), at a gain of $110,400.17 less sales and advertising expense of $5,297.30, and in 1947, he sold 49 more at a gain of $135,911.03 (R. 34).

On October 19, 1949, the taxpayer still owned approximately 120 of the 291 houses he had acquired from the corporation (R. 32).

From the foregoing evidentiary findings, the Tax Court found as an ultimate fact that in 1946, when the sales of the houses in question were made, the property was "held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business." (R. 35).

The Tax Court accordingly sustained the deficiency determination made by the Commissioner (R. 11, 23, 35, 36). The Court of Appeals affirmed (R. 100).

ARGUMENT

The unchallenged findings of the Tax Court demonstrate that from the time taxpayer acquired half the stock in the J. L. Martin Investment Company to and throughout his acquisition of sole ownership of the real property in question, his purpose was to sell. That was not a new-found purpose forced upon him by any change in the property's income potential. Rather, from the beginning, he proposed to engage in the business of selling to anyone who would buy, whenever and however, he could. Thus, shortly after the taxpayer became president of the corporation, in 1943, letters were addressed to the tenants then occupying the houses, expressing the

corporation's desire to sell the property. And as taxpayer himself testified (R. 87):

> I went out looking for opportunities to sell them in 1945 and in 1946 when the VA made it possible. That was March, 1946, first time sales were possible.

Consequently this case is a far cry from what the petition for certiorari now seeks to make it out to be. The taxpayer was engaged in no mere liquidation of a property which had ceased to be income-producing, as in *Three States Lumber Co.* v. *Commissioner,* 158 F. 2d 61 (C.A. 7th). Nor did the facts here call for, permit of, or elicit the announcement by the court below of a general principle that "if an owner of property is not engaged at all in buying and selling any properties, but decides to sell some that require any sales effort, he automatically becomes engaged in the trade or business of selling properties and they cease to be capital assets." (Pet. 9-10).

In short, this case presents no disputed question of law but only the application of plain statutory language to the particular facts in this record. The Tax Court found that the sales "in question were made *to customers* in the *ordinary* course of his business" (R. 34) (italics supplied). That finding was plainly not clearly erroneous and so the court below quite properly sustained it. There is obviously no occasion for further review. See also

the Government's Brief in Opposition in *Rubino* v. *Commissioner,* No. 53, this Term, involving a similar factual situation.

CONCLUSION

The decision of the court below is not in conflict with any other decision. It is a correct interpretation of the taxing statute and presents no question of importance. It is, therefore, respectfully submitted that the petition for a writ of certiorari should be denied.

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